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THE INSURANCE TRUST AS NON-TESTAMENTARY DISPOSITION

By ORVILLE F. GRAHAME*

ONE of the problems that is most often raised in connection with the life insurance trust is whether it is a testamentary disposition and should therefore be attested in accordance with the requirements of the statute of wills.¹ As a business matter it is generally not so attested, and thus the question involves the basic validity of millions of dollars of life insurance now held in trust.² The question does not have reference to funds held under the options of settlement contained in insurance policies as these options create a debt and not a trust³ but rather refers to policies payable to a trustee as beneficiary or assignee.

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¹For other discussions of this problem, see Phillips, *Life Insurance Trusts*, (1933) 81 U. of Pa. L. Rev. 284, 408; Davis, *The Statute of Wills and Life Insurance*, (1931) 5 Ass'n of Life Insurance Counsel Proceedings 203; Horton, *The Testamentary Nature of Settlements of Life Insurance Elected by the Beneficiary*, (1931) 17 Corn. L. Q. 72, 77; Horton, *Life Insurance Trust Handbook* (1933) 22; Scott, *Cases on Trusts*, 2d ed., 802; Fraser, *Personal Life Insurance Trusts in New York*, (1930) 16 Corn. L. Q. 19, 30; Yost, *Some Problems Relating to Life Insurance Trusts*, (1930) 4 Ass'n of Life Insurance Counsel Proceedings 567; Peterson, *The Assignment Route or Beneficiary Route to Life Insurance Trusts*, (1931) Proceedings of the Legal Section American Life Convention 58; note (1933) 46 Harv. L. Rev. 818. A case involving this problem was argued before the supreme court of the Ames Competition of the Harvard Law School, and a copy of the Briefs and Record were kindly loaned to the writer by the editor of the Harvard Law Review. The Record is dated November 19, 1932.

²In 1929 it is said that more than two per cent or \$2,500,000,000 of American life insurance was in trust. Scully and Ganse, *Business Life Insurance Trusts* 29. At the end of 1930 about four per cent or \$4,000,000,000 was held in trust. (1932) 45 Harv. L. Rev. 896. Due to the present economic situation it may be assumed that there has been a decrease in this amount.

³Vance, *Insurance*, 2nd ed., 609; Horton, *Power of an Insured to Control the Proceeds of his Policies* 49; Bogert, *Some Recent Developments in the Law of Trusts*, (1929) 23 Ill. L. Rev. 749, 754; note (1927) 36 Yale L. J. 394; Danziger, *Does the Rule Against Perpetuities, and Do Statutes Modifying that Rule, Affect Life Insurance Policies and Their Proceeds*, (1930) 4 Ass'n of Life Insurance Counsel Proceedings 467. In some states insurers are permitted by statute to be trustees. Vance, *Insurance*, 2nd ed., 609. Some writers say a trust exists. Madden, *Wills Trusts and Estates* 82; Van Hecke, *Insurance Trusts, The Insurer as Trustee*, (1928) 7 N. C. L. Rev. 21. See also *New York Life Ins. Co. v. O'Brien*, (D.C. Mich. 1927) 27 F. (2d) 773; (1929) 77 U. of Pa. L. Rev. 430; Cronbach

The view that the life insurance trust is a testamentary disposition of property is based upon the indisputable fact that in many cases the insured reserves many rights to himself while purporting to create a title in the trustee. If title is transferred by assignment, there is the possibility that such assignment is conditioned to take effect only if the insured predeceases the trustee-assignee. If the beneficiary method is used, a difficulty arises by reason of the many reservations of rights to the insured, such as the right to revoke the trust and to change the beneficiary, or to get the cash, loan or other value. Along with this reservation of rights by the insured-settlor is the further fact that the trustee, it would seem, is given very little title to the so-called trust property and has no important duties during the lifetime of the insured. On the death of the insured a fund comes into the hands of the trustee, free from all but the trust restrictions, and it is debated whether this is in effect a testamentary disposition. Cases are cited, and justifiably so, which hold that an individual cannot pretend to declare property in trust and retain all dominion over such property.

Much of the confusion that has developed is due to the failure to recall that the life insurance trust is not a new device and the failure to appreciate that the development of the rights of a third party beneficiary under a life insurance policy has been somewhat unique and decidedly circuitous. A brief account of the history of the insurance trust and the emergence of the rights of the third party beneficiary will assist materially in an understanding of the problem involved.

While the life insurance trust as a regular commercial enterprise has been a development in the United States since 1920,⁴ it is as a matter of fact about as old as the institution of life insurance itself. The trust institution antedates⁵ the statute of uses⁶ enacted in 1535. The trust concept was well accepted in America prior to 1800.⁷ Life insurance developed after the trust, and the trust arrangement no doubt was soon employed in connection with the new form of property based on contract. In 1706 an attempt

v. *Aetna Life Ins. Co.*, (1926) 153 Tenn. 362, 284 S. W. 72; (1927) 36 Yale L. J. 394.

⁴Hanna, *Some Legal Aspects of Life Insurance Trusts* (1930) 78 U. of Pa. L. Rev. 346; Scully and Ganse, *Business Life Insurance Trusts* 26.

⁵Bogert, *Trusts* 9.

⁶27 Henry VIII, ch. 10.

⁷Bogert, *Trusts* 15.

was made in England by the Amicable Society for a Perpetual Assurance Office to offer insurance, but the first life insurance offered on a scientific basis was by the Equitable Assurance Society of London established in 1762.⁸ There is a record of a life insurance policy having been placed in trust on April 23, 1787,⁹ and it is not likely that this was the first life insurance trust.

There are a number of English and Irish cases involving life insurance trusts decided prior to 1850. The case of *Glynn v. Locke*¹⁰ decided in 1842 involved a trust dated September 27, 1808. It was declared in another Irish case in 1854 that "it is at present one of the most ordinary arrangements in marriage settlements to have a policy of assurance effected to secure some portion of the settled fund, and to have that policy vested in the trustees on certain specific trusts."¹¹ An English case decided in 1889, *Bridger v. Deane*,¹² involved a funded insurance trust dated March 20, 1834, and the policy was issued in 1830.

Life insurance didn't get under way until about 1850¹³ in the United States, but it may be assumed that very soon thereafter the trust arrangement was used in connection therewith. The supreme court of Maine in 1878 had before it a case¹⁴ involving a policy dated January 1, 1866, payable in trust, and this may possibly be as old a life insurance trust arrangement as there is a record of in the United States.¹⁵ That the life insurance trust was employed again and again in cases where it was needed is evidenced by the numerous cases involving policies payable in trust adjudicated by the courts of last resort of the several states.¹⁶ In

⁸Vance, Insurance, 2nd ed., 22.

⁹Courtney v. Ferrers, (1827) 1 Sim. 137, 5 L. J. O. S. Ch. 107. This policy was issued by the Equitable Assurance Office.

¹⁰(1842) 5 Ir. Eq. 61.

¹¹Ford v. Ryan, (1854) 4 Ir. Ch. 342.

¹²(1889) 42 Ch. D. 9, 61 L. T. 492, 37 W. R. 786.

¹³Vance, Insurance, 2nd ed. 22.

¹⁴Cables v. Prescott, (1878) 67 Me. 582.

¹⁵A trust dated June 13, 1869, with what is now the Girard Trust Company as trustee, has been mentioned as the oldest heretofore known life insurance trust. Hanna, Some Legal Aspects of Life Insurance Trusts, (1930) 78 U. of Pa. L. Rev. 346; Scully and Ganse, Business Life Insurance Trusts 26.

¹⁶Contrary to the opinion of some, there are a considerable number of cases, approximately a hundred, which involve the life insurance and trust relationship. More than half of the state jurisdictions have passed on the life insurance trust. One of the first American cases was that of Bond v. Insurance Co., (1873) 9 Phila. (Pa.) 149. The supreme court of California had a life insurance trust before it in 1877 in the case of Silvey v. Hodgdon, (1877) 52 Cal. 363. Space will not permit citing other cases

fact, it is entirely clear that the life insurance trust, about which there has been much concern recently, preceded the development of the American doctrine of the rights of the third party beneficiary under a life insurance policy.¹⁷

With few exceptions, which will be noted later,¹⁸ the life insurance trust has been enforced by the American courts,¹⁹ and where the question has been raised the trust has been held to be non-testamentary.²⁰ It was when the trustee took the position of payee under the modern policy, with its reservation of rights to the insured, a position generally held by a donee beneficiary, that question was made as to whether the trustee possessed any title to a res upon which to predicate a trust. To answer this problem it is necessary to determine the nature of the rights, if any, of a third party beneficiary during the lifetime of the insured.

It would seem that when life insurance first developed in England the policy was owned by the insured and was payable in effect to his estate.²¹ One of the most natural steps for the insured to take was to assign the policy in trust for the benefit of persons he cared to provide for. As was stated previously, this was commonly done in marriage settlements.²² The English people engaged much in shipping, and their insurance followed the development of marine insurance.²³ While there is evidence that wager policies, based on no interest in the assured, were not uncommon, it was soon declared that life insurance policies must be upon the lives of those in whom the one effecting the insurance had an insurable interest,²⁴ as he might have an insurable interest in a cargo. In such cases the life insurance contract was made between the company and the person possessing the insurable interest, who became the beneficiary. But this party was not a third party donee beneficiary but rather an owner beneficiary be-

dealing with the trust, except those having a particular bearing on the testamentary problem.

¹⁷The Hume Case, which laid the foundation for the rights of a third party beneficiary, was not decided until 1888. *Central Nat'l Bank v. Hume*, (1888) 128 U. S. 195, 9 Sup. Ct. 41, 32 L. Ed. 370.

¹⁸*Infra* notes 58 and 59.

¹⁹*Supra* note 16.

²⁰See cases discussed subsequently in this article.

²¹The money paid by the Amicable Society for a Perpetual Assurance Office organized in 1706 was paid to the representatives of each member dying. *Vance, Insurance*, 2nd ed., 22.

²²*Ford v. Ryan*, (1854) 4 Ir. Ch. 342.

²³*Vance, Insurance*, 2nd ed., 14, 15.

²⁴*Vance, Insurance*, 2nd ed., citing 19 Geo. II, ch. 37, and 14 Geo. III, ch. 48.

cause he was a party to the contract and paid the consideration therefor.

Life insurance was introduced into the United States at a time when this was the status of the beneficiary's rights. In Bliss on Life Insurance published in 1872²⁵ it was stated that in the opinion of the author, though there were no cases, the United States courts would hold a life policy to be an irrevocable trust, although a different rule prevailed in England. Professor Vance cites Connecticut, New Jersey and Louisiana as holding in 1871, without the aid of statutes justifying previous decisions in other states, that the interest of a donee-beneficiary was vested and could not be defeated by the insured who was the promisee under the contract.²⁶ Mr. Boughton cites Indiana and Minnesota as being the first states to adopt the view held by Mr. Bliss.²⁷ The United States Supreme Court adopted his language in 1888 in the celebrated case of *Central National Bank v. Hume*,²⁸ and thus established the rule. Chief Justice Fuller stated:

"It is indeed the general rule that a policy, and the money to become due under it, belong, the moment it is issued, to the person or persons named in it as the beneficiary or beneficiaries, and that there is no power in the person procuring the insurance by any act of his, by deed or by will, to transfer to any other person the interest of the person named."

The rule of this case has been distinguished on the ground that it applies only to contracts made in fact with the beneficiary,²⁹ but its more general language has become firmly rooted in our law,³⁰ though the rule is said not to exist elsewhere.³¹ The English rule by statute provides only that a husband may insure himself for the benefit of his wife and children, the policy to enure to them and to be deemed a trust.³² In Canada ordinary third party beneficiaries by statute may be eliminated at will, while beneficiaries for value, and preferred beneficiaries, a certain group of relatives, possess something in the nature of a vested right though the in-

²⁵1st ed., sec. 317.

²⁶Vance, Insurance, 2nd ed., 554.

²⁷Boughton, Creditors and Surrenders, (1926) 3 Ass'n of Life Insurance Counsel Proceedings 311.

²⁸(1888) 128 U. S. 195, 9 Sup. Ct. 41, 32 L. Ed. 370.

²⁹Boughton, Creditors and Surrenders, (1926) 3 Ass'n of Life Insurance Counsel Proceedings 311. *Vorlander v. Keyes*, (C.C.A. 8th Cir. 1924) 1 F. (2d) 67; *In re Whiting*, (D.C. N.C. 1925) 3 F. (2d) 440.

³⁰See any digest of cases, such as 37 C. J. 577, 578.

³¹Vance, Insurance, 2nd ed., 551-553.

³²45 & 46 Vict. ch. 75, sec. 11.

sured may shift the beneficiary designation from one preferred beneficiary to another.³³

A number of bases for the American view have been given,³⁴ but the important fact is that the beneficiary was in effect declared the owner. Only Wisconsin demurred.³⁵ In the early days of the rule there were no loan or cash values or annual dividends to confuse the issue. Under this view of the rights of a beneficiary the declaration of a policy in trust by naming the trustee beneficiary did not raise any question of testamentary disposition. The beneficiary took a present existing title to the policy.³⁶

But this view of the courts does not fit the present day concept of a policy as being the property of the insured, and it is natural that many courts have in the past quarter century taken the view that if the right is reserved to change the beneficiary the beneficiary has only contingent rights, some say an expectancy only, which becomes vested only on the death of the insured.³⁷ But not all courts have unqualifiedly adopted this view. It is not clear that even a majority have. In fact, there are conflicting decisions in a given jurisdiction.³⁸ The result has been that many courts have only reluctantly recognized the rights of the insured and have held that a third party beneficiary has such rights in a policy as to require any party dealing therewith, if the interest of such beneficiary is affected, to deal in accordance with the terms of the policy.³⁹ The beneficiary is said to have vested

³³Foster, *The Uniform Life Insurance Laws of the Canadian Provinces*, (1924) 2 Ass'n of Life Insurance Counsel Proceedings 473.

³⁴For instance: (1). The statutes authorizing insurance for the benefit of a wife. 37 C. J. 577 n. (2). The theory of a gift of a chose in action. (3). The theory of the insured acting as agent for the beneficiary in arranging for the insurance. (4). The theory of a trust declared by the insured-promisee when he takes the insurer's promise for the use of the beneficiary. Vance, *Insurance*, 2nd ed., 554-556.

³⁵Clark v. Durand, (1860) 12 Wis. 223, modified by statute as to married women. Wisconsin Statutes, 1898, sec. 2347.

³⁶In an early North Carolina case, citing Bliss, *Life Insurance*, 2nd ed., 517, it was said that a life policy created a vested interest in the beneficiary, and that while the rules for interpreting a will may guide, as far as they are applicable, in ascertaining the legal effect of a life insurance clause, there was a difference in that the interest vests under the policy at once upon its issue, while under a will the interest vests only on the death of the testator. Hooker v. Sugg, (1889) 102 N. C. 115, 8 S. E. 919.

³⁷37 C. J. 579, 580.

³⁸Holland, *Assignment by the Insured of Policies which Reserve to the Insured the Right to Change the Beneficiary*, (1929) 4 Ass'n of Life Insurance Counsel Proceedings 181.

³⁹Holland, *Assignment by the Insured of Policies which Reserve to the Insured the Right to Change the Beneficiary*, (1929) 4 Ass'n of Life Insurance Counsel Proceedings 181.

rights subject to be divested, but only by the insured's exercising the power of divestment as agreed.

This rule would prevent an insured, unless the policy expressly gave him that right, from surrendering a policy, from getting the loan value, from assigning the policy so as to cut out the beneficiary, and from a mutual rescission, without the consent of the beneficiary. Under this rule the reservation to the insured of one of these rights, such as the right to change the beneficiary, does not carry with it the right to do some other act, such as the right to elect to take the cash value.⁴⁰

Where this rule obtains, the naming of a trustee as beneficiary would create a vested interest, though subject to divestment, in the trustee, and a question of testamentary disposition should not arise.⁴¹ If the assignment method is used, care would have to be taken to effect transfer of title to the beneficiary, which would undoubtedly require, in the absence of a policy provision permitting an assignment to act as a change of beneficiary, a joinder by any existing beneficiary or a preliminary change to the insured's estate.⁴²

It is where the view that the beneficiary has contingent or expectant rights obtains that the problem of testamentary dispositions principally arises. Where this rule exists, however, if the right to change the beneficiary is not reserved, the beneficiary is said to have vested rights,⁴³ and in such a case, as in the case above and as under the *Hume Case*, there would not be any question of a testamentary disposition. The complainants seeking to invalidate a life insurance trust in *Gurnett v. Mutual Life Insurance Co.*⁴⁴ recognized that this result would follow, if the right to change the beneficiary had not been reserved.

In this connection, before giving consideration to the theories and cases having a direct bearing on the testamentary problem, where the trustee is a third party beneficiary in a state in which it is said the beneficiary has only expectant or contingent rights, it

⁴⁰Hill v. Capitol Life Ins. Co., (1932) 91 Colo. 300, 14 P. (2d) 1006; Grahame, The Rights of a Beneficiary, (1933) 2 Ins. Dec. 318.

⁴¹Note (1933) 46 Harv. L. Rev. 818.

⁴²See *Anderson v. Broad Street National Bank*, (1918) 90 N. J. Eq. 78, 105 Atl. 599. This is a rule that works both ways: a trustee beneficiary is not necessarily cut out, completely at least, by assignment even though the policy is withdrawn from the trust. *Bose v. Meury*, (1932) 112 N. J. Eq. 62, 163 Atl. 276.

⁴³See 7 Cooley, Briefs on Insurance 6399ff.

⁴⁴(1932) 268 Ill. App. 518.

must be understood that the problem is essentially one pertaining to the rights of a third party beneficiary and that only as such does it affect life insurance trusts. In other words, it is submitted that if a life insurance policy payable to a third party beneficiary is not testamentary, a life insurance trust is not, for in both cases legal title to the insurance funds is given by the policy to the designated beneficiary.⁴⁵ In the case of a trust a split property interest is involved, but this is a trust problem, not a problem in wills.

It must also be understood that a life insurance contract is not in itself testamentary where it is payable to the insured, or to a party who is the owner and the promisee as a result of being the only other party to the contract. In the first case the problem could hardly arise since the policy would always be available for estate purposes. In the second case ownership rights are always in the promisee-beneficiary, and they are never in the insured and do not vest upon his death; the death is merely an event determining the date of payment.

It is seen that under the old view of the third party beneficiary as owner, the same result would be reached for the same reason, namely, that the rights from first to last exist in the beneficiary.⁴⁶ This view, as previously explained, still obtains in modified form in many of the states.⁴⁷ Though the view may be something of an anomaly, it is indeed not without merit.

Were it not for the above situations being indisputably non-testamentary, the entire problem could be dismissed because life insurance contracts are buttressed by countless statutes which have a dignity equal to that of the statutes on wills. But as the matter stands, it may be contended that most of such statutes have reference only to the clearly non-testamentary life insurance contracts. Some of the life insurance statutes do, however, apply to all insurance contracts including those alleged to be testamentary, such as the statutes in the "insured as owner" states, where the beneficiary has only contingent rights, providing for exemption from claims of creditors even where the right to change the bene-

⁴⁵See *Bose v. Meury*, (1932) 112 N. J. Eq. 62, 163 Atl. 276, which pointed out that the trustee took its title to the insurance money under the policy, and *Gurnett v. Mutual Life Ins. Co.*, (1932) 268 Ill. App. 518, where the problem was disposed of by holding the trustee to be a donee-beneficiary.

⁴⁶*Supra* note 36.

⁴⁷*Supra* notes 38 and 39.

fiary is reserved. These statutes would prevent any claim from being filed by the creditors on the ground that the contract is testamentary and thus void, but they would not prevent the heirs and legatees from filing a claim. As to this possibility, and as to the possibility of claims by creditors in states having no exemption or a limited exemption statute, recourse must be had entirely to general principles.

It may be concluded that life insurance trusts as well as life insurance contracts will not be held to be testamentary even though the trustee is named as third party beneficiary. Though the authorities for the most part are general on both situations, and have not clearly expounded the legal and historical principles involved, it would seem there are too many cases upholding and dealing with both the life insurance trust⁴⁸ and the life insurance contract⁴⁹ payable to the third party beneficiary for most courts to take any view other than to uphold their validity.

The general principle to support the trust or contract theoretically might very well be a general announcement of a strong contingent interest in the beneficiary⁵⁰ during the lifetime of the insured which the insured may freely cut off but which exists until cut off, and which is contingent only because it can be cut off. This will really be a vested interest subject to easy divestment, rather than a vested interest subject to most difficult divestment, the rule obtaining in many states. This interest would be more than a hope or mere expectancy. It is said that contingent interests may be assigned in trust.⁵¹ In considering this interest the old theory of beneficiary as owner must not be forgotten as a background for the strong contingent interest. While it has been often said that the beneficiary has but an expectant interest⁵² and on occasion this interest has been compared to the interest of an heir or legatee,⁵³ it is submitted that "expectant" has generally not been

⁴⁸Supra note 16.

⁴⁹See cases in any digest on rights of beneficiaries, such as 37 C. J. 576, 588. It has been declared that a life insurance contract is not testamentary. *Martin v. Modern Woodmen of America*, (1912) 253 Ill. 400, 97 N. E. 693; *Hooker v. Sugg*, (1889) 102 N. C. 115, 8 S. E. 919; *Johnston v. Scott*, (1912) 76 Misc. Rep. 641, 137 N. Y. S. 243; *Lehman v. Lehman*, (1905) 29 Pa. Super. Ct. 60.

⁵⁰The beneficiary's interest is sometimes said to be contingent. See 37 C. J. 580.

⁵¹Perry, *Trusts and Trustees*, 7th ed., sec. 69; Scott, *Trusts and the Statute of Wills*, (1930) 43 Harv. L. Rev. 521, 528 n. 19.

⁵²Vance, *Insurance*, 2nd ed., 561, 562.

⁵³*Supreme Council American Legion of Honor v. Gehrenbeck*, (1899) 124 Cal. 43, 44 Pac. 640.

used in this sense, but rather in the sense of "contingent." Some courts in trying to free the life insurance policy from the stranglehold of the theory of the beneficiary having a vested interest have used language to belittle the beneficiary's interest that was not necessary or well-considered. Nevertheless their declarations have been such that it would not be difficult to decide that by expectant they meant contingent.

The theory of contingent interest was dealt with in *Hirsh v. Auer*⁵⁴ by the court of appeals of New York in 1895. This case upheld the life insurance trust. The court said:

"The fact that the trust dealt with a contingent interest of the insured in the certificate of insurance is of no moment. That interest became vested at the death of the insured, and, the beneficiary having collected the insurance money, the trust, under the agreement creating and acknowledging it, attached to the fund. A trust of this character is not to be distinguished from assignments of contingent interests, which courts of equity recognize as valid."

This case involved a benefit certificate, and the rule as to vested rights of the beneficiary was never extended to such certificates.⁵⁵ Thus, while the court only referred to the insured's contingent interest, any mention of the beneficiary's interest would likewise not have been to any vested interest of such beneficiary.

In *Kerr v. Crane*⁵⁶ the supreme court of Massachusetts in 1912 made a strong pronouncement that a trust of an insurance benefit certificate could not be avoided on the ground that it was testamentary. This court considered the question from both the insured and the beneficiary angles. It declared:

"It is said that the interests both of the insured member and of this beneficiary were merely contingent and not actually vested rights of property in an existing fund. That is true. The amount of the benefit might never be realized at all. If it were to be realized, yet the member had no other interest therein than the bare power to appoint some person of a limited class to receive the fund if and when it should become due and payable. The beneficiary had no other interest than a mere expectancy dependent upon the will and pleasure of the insured member. But it does not follow that the holder of such a merely expected or contingent interest, growing or expected to grow out of actually existing, though defeasible, contractual rights, has no power of dealing with it, or that his engagements made with reference to such an inter-

⁵⁴(1895) 146 N. Y. 13, 40 N. E. 397.

⁵⁵Vance, Insurance, 2nd ed., 586-588.

⁵⁶(1912) 212 Mass. 224, 98 N. E. 783.

est while it is merely expectant and contingent, may not be enforced in equity after the interest shall have become vested and absolute. And it has been so held with reference to just such contingent and expected rights as are here in question."

It will be noted that the *Hirsh* and *Kerr* cases were applying something more than a rule involving contingent interests, subject to divestment. They were also applying the rule that equitable rights attached to the fund when it came into existence. They were probably not bothered so much by the problem of testamentary dispositions for the insured under a benefit certificate at this time generally had no cash rights during his lifetime which ceased or passed on his death. The reasoning of these courts has been applied to War Risk Insurance, where the court said:

"Nor are we persuaded that the line of cases against mortgages on property which has no potential existence applies to the present case, for, while the trust fund was contingent, it became vested upon the death of the insured, and became subject to the trust ingrafted thereupon."⁵⁷

The supreme court of Kansas, however, by a divided court, laid much stress on the fact that the War Risk Insurance fund was not in existence, and that an attempted gift was not complete and executed and beyond the power of revocation.⁵⁸ The court added:

"So far as the elements of a trust entered into the transaction, it was executory in character and in some respects had the elements of a testamentary bequest subject to change or revocation without the consent of those to whom the tentative gifts had been promised."

And in a Georgia case⁵⁹ where the insured had referred by letter to the disposition of the money to be collected after his death, the court held that this was not a change of beneficiary or assignment, and that if the money referred to was his property such letter was testamentary. The court refused to create a trust for the same reason.

These last two cases would seem to require a specific property interest in the trustee during the lifetime of the insured, but this should be supplied by an interest vested, subject to divestment, or a contingent interest, contingent only because it may be revoked. In view of the many theoretical possibilities, and in view of the

⁵⁷*Lashley v. Lashley*, (1924) 212 Ala. 255, 102 So. 229; accord as to this kind of insurance, *Ambrose v. United States*, (D.C. N.Y. 1926) 15 F. (2d) 52; *Christensen v. Christensen*, (D.C. N.Y. 1926) 14 F. (2d) 475.

⁵⁸*Staples v. Murray*, (1928) 124 Kan. 730, 262 Pac. 558.

⁵⁹*Bennett v. Rosborough*, (1923) 155 Ga. 265, 116 S. E. 788.

general rules applying to rights of beneficiaries, it would seem that the opinions in these cases are unimaginative and will not be generally controlling. It would be surprising if they were followed in their own jurisdictions. It has been declared that the trustee has a present interest.⁶⁰

Another viewpoint that should be considered in disposing of this problem, and to reconcile the beneficiary-as-owner and the insured-as-owner views, is that both the insured and the beneficiary have different rights in a policy, each independent of the other. A life insurance contract is of a multiple nature in that it creates a number of rights. These rights in the modern policies may be divided into those held by the insured and those held by the beneficiary. The insured has the right to the cash and loan values and to the dividends, while the beneficiary owns the promise to pay at death, subject to a right of revocation in the insured. This right of the beneficiary is of real substance, and is the major right given in the policy and gives effect to the primary purpose of life insurance. The right to cash and loan values are secondary rights now required by statute to avoid forfeiture, and arise out of the nature of the legal reserve system. The right to a dividend is similarly the result of the cooperative and mutual nature of a conservative insurance enterprise. A life insurance policy is a very illogical arrangement indeed divorced from its one great primary obligation to pay the beneficiary the face amount of the policy on the death of the insured.⁶¹ In some respects this dual character of a life insurance policy is not unlike a life estate to the insured with a vested remainder to the beneficiary, subject to be divested by the beneficiary's prior death, or by the insured's revocation.

⁶⁰*Gurnett v. Mutual Life Ins. Co.*, (1932) 268 Ill. App. 518; *Johnston v. Scott*, (1912) 76 Misc. Rep. 641, 137 N. Y. S. 243. The last case contains the statement: "the trustee had a present title, and the beneficiary had a vested interest, subject to be divested by the power of revocation." In other language the court indicated that the insured was in effect trustee during his lifetime. Cf. *infra* note 70.

It has been maintained, if the trustee is beneficiary with right of revocation, that during the lifetime of the insured there is no title in the trustee and that no trust exists. *Fraser, Personal Life Insurance Trusts in New York*, (1930) 16 *Corn. L. Q.* 19, 30. It has also been maintained that in measuring lives in being you do not therefore need to count any life until insured's death. *Remsen, Preparation of Wills and Trusts*, 2d ed., 321. But if the trust is revocable a suspension of alienability may not result. *Equitable Trust Co. v. Pratt*, (1922) 117 Misc. Rep. 708, 193 N. Y. S. 152, *aff'd* (1923) 206 App. Div. 689, 199 N. Y. S. 921; *Pulitzer v. Livingston*, (1896) 89 Me. 359, 36 Atl. 635; note (1933) 45 *Harv. L. Rev.* 896.

⁶¹*Boughton, Creditors and Surrenders*, (1926) 3 *Ass'n of Life Insurance Counsel Proceedings* 311.

This rule that the beneficiary, the trustee, does not take any of the insured's rights, but takes his own, received support in the recent New Jersey case of *Bose v. Meury*.⁶² However, it is not clear that the court considered that these rights had any existence until the insured's death, and if this was the case the doctrine of the *Hirsh* and *Kerr* cases, of the trust attaching to the found when it came into existence, would have to be considered in connection with such view. However, in view of the staunch support given by New Jersey to beneficiary rights, the state often holding that to divest the large rights of the beneficiary the procedure prescribed in the policy must be followed, it may be assumed that the beneficiary trustee was considered to have had rights during the insured's lifetime. Even the *Bose Case* held, as had previous cases, that an assignment did not divest the beneficiary of his rights.

In considering that the beneficiary had separate rights the *Bose Case* declared that the trust is really established by the beneficiary of the policy, the trustee. To the claim that there was no parting with the subject matter and that the insurance trust was testamentary, the court said:

"Whatever merit there may be to the points, were the res in trust the property of the trustor, they are beside the question where, as here, the res is the proceeds of insurance on the life of the trustor which never were his property. The proceeds are the fulfillment of promises by the insurance company to the Montclair Trust Company, trustee, to pay the stipulated sums, upon the death of the insured. The insured paid the consideration for the promises and he had the right, under the terms of the policies, to change the promises at will, but when the day came—the insured's death—the obligations of the insurance company were due to the Montclair Trust Company, trustee. Its source of title was the promise in the policies, not the trust agreement. The trust agreement is no more than a declaration of trust by the trustee that it would hold the proceeds of the policies for the benefit of the insured's wife and children, and whether it had physical possession of the policies or whether there was a stripping of interest by the 'donor', or that the trust deed was testamentary, is wholly immaterial."

Under this language the trust was sustained, but the way was still left open to contend that the policy, which gave the trustee his title, was testamentary. But due to the prevailing view in New Jersey, as indicated above, such a contention would probably be unsuccessful in that state.

The view that the beneficiary-trustee declares the trust, though

⁶²(1932) 112 N. J. Eq. 62, 163 Atl. 276.

no cases were cited, is not exactly new. Where a trustee has already been named beneficiary before a trust is declared, it would appear that the real declaration of trust is by the beneficiary and not the insured, since title is already in the beneficiary, who is to be trustee. There are several cases where this would seem to have been the basis of the trust though no direct mention was made of such basis.⁶³ In several other cases it is clear that had the beneficiary acted a trust would have been sustained.⁶⁴ Several cases have expressly declared that the trust was declared or recognized by the beneficiary-trustee.⁶⁵ In the absence of such action the general rule is applied that the declarations of a grantor to create a trust must be made prior to, or contemporaneous with, the vesting of rights under the instrument under which the trust is claimed.⁶⁶ Some courts have indicated that the basis of the trust, considering the attitude of the trustee, is something created by the courts to prevent the trustee-beneficiary from gaining by his wrong, equity raising a trust *ex maleficio* against such trustee.⁶⁷ In situations similar to these where the beneficiary-trustee is responsible for the trust, it is not likely that the trust will be held testamentary since the trust could be invalidated only by declaring the policy testamentary.

There is a view related to that expressed in the *Bosc Case* which would prevent any possibility of a life insurance contract or trust from being criticised as testamentary on the usual grounds. This view is that the insurance fund was never owned by the insured or beneficiary until it accrued to the beneficiary on the death of the insured, the death being the event which under the contract

⁶³*Devries Estate v. Hawkins*, (1903) 70 Neb. 656, 97 N. W. 792; *Alexander v. Woodmen of the World*, (1916) 193 Mo. App. 411, 186 S. W. 2; *Levin v. Ritz*, (1895) 17 Misc. Rep. 737, 41 N. Y. S. 405.

⁶⁴*Fee v. Wells*, (1918) 65 Colo. 348, 176 Pac. 829—"There is no claim or evidence that the beneficiary declared a trust and constituted herself trustee." *Manley v. Manley*, (1901) 107 Tenn. 191, 64 S. W. 8.

⁶⁵*Lashley v. Lashley*, (1924) 212 Ala. 255, 102 So. 229—"Moreover, while it may not have been necessary, the bill charges an express recognition of the trust by the trustee subsequent to the death of the insured;" *Makowiec v. Prudential Ins. Co.*, (1929) 83 N. H. 547, 145 Atl. 269.

⁶⁶*Michigan Mutual Life Ins. Co. v. Liphart*, (1913) 177 Ill. App. 645; *Bennett v. Rosborough*, (1923) 155 Ga. 265, 116 S. E. 788; *Fee v. Wells*, (1918) 65 Colo. 348, 176 Pac. 829.

⁶⁷*Coyne v. Supreme Conclave*, (1907) 106 Md. 54, 66 Atl. 704. "There is also a class of trusts which arise *ex maleficio*, and equity in order to reach the possessor of what in conscience belongs to another turns him into a trustee." See also *Gurnett v. Mutual Life Ins. Co.*, (1932) 268 Ill. App. 518; *Cockrell v. Cockrell*, (1902) 79 Miss. 569, 31 So. 203; *Matter of Will of O'Hara*, (1884) 95 N. Y. 403 (not involving insurance trust).

determined the rights, which rights had no previous existence and could not possibly pass on insured's death. This view received considerable support in the New York case of *Matter of Haedrich*.⁶⁸ The court stated that a policy payable to the estate of the insured was subject to the transfer tax only because

"the proceeds of the transaction are beyond the protecting shield of public policy, and not, as stated in certain cases, because they pass under the will or the intestate laws of the state, since the latter is not the case in any true sense. The right to receive the money on the insurance in any such case does not pass by will or intestate laws. The right accrues to individuals who answer a certain description specified in the contract, but it is not a right decedent ever possessed, and it is fundamental that non dat qui non habet."

If the decedent, the insured, never possessed that right, apparently the beneficiary was not considered as having any rights until the insured's death, for here the insured was the beneficiary of his own policy. Under such a view it would make no difference how bare an expectancy the beneficiary has; his rights would accrue under contract obligations when a certain event occurs, the death of the insured, and would never be owned by the insured so as to pass on his death. This situation would be much like that where the beneficiary is the owner of the policy, for in such a case the death merely determines the contract obligations. Under this view the transaction looks testamentary where there is a third party beneficiary because the determining event is the death of one of the contracting parties. It would not look so much this way if the contract was between A and B to pay C a given sum upon the death of X.

Due to the fact that one of the most accepted theories as to the origin of the vested rights of the beneficiary is the theory of a declaration of trust by the insured,⁶⁹ it is somewhat surprising that there has not been more said in regard to this problem about the insured acting as trustee during his lifetime, and being superseded on his death by the trustee-beneficiary. Thus, it could be said that if the insured retains extensive rights of ownership, certain of these are held in trust as declared. A few of the cases have given some indication of this. In *Johnston v. Scott*, decided

⁶⁸(1929) 134 Misc. Rep. 741, 236 N. Y. S. 395, aff'd (1931) 256 N. Y. 608, 177 N. E. 160.

⁶⁹Vance, Insurance, 2nd ed., 551ff.

by a lower court in New York in 1912,⁷⁰ the court declared regarding an insurance trust:

"The property is personal; the declaration of the trust by the settlor impressed it with a trust character and converted his legal title to that of trustee for the person for whose benefit the trust was created."

This is important because the court added in regard to testamentary dispositions:

"That the trust created was not to take effect in possession and enjoyment until the death of the settlor was because of the nature and source of the property and the terms of the deed, not because the deed or transaction was testamentary in character."

In other language, previously referred to, however, the court spoke of the trustee having a present title.

In another case, where an attempted assignment to children was frustrated by the company, it was held that such action amounted to a declaration in trust for the children. The court said:

"It would be hard to conceive of circumstances that would furnish stronger reasons for the application of the principle of constructive delivery and acceptance for the donees by the donor as their trustee."

Therefore, the insured, was not permitted to disavow the trust.⁷¹ In cases of defective assignments in trust the courts have looked for an intention on the part of the insured to hold himself as trustee.⁷² It has been held that an insured may name his estate in trust for his heirs, and that the creditors cannot take, and that this does not violate the statute of Wills.⁷³ In such a case any rights necessary to the existence of the trust during the insured's lifetime would have to be held by him. Where an insured names himself in violation of an agreement he is declared a trustee.⁷⁴ In England, however, the theory of the insured holding in trust has made little headway, even to the extent of creating ordinary third party beneficiary rights.⁷⁵

Before leaving the problem of a trustee as beneficiary, mention should be made again of the recent case of *Gurnett v. Mutual*

⁷⁰(1912) 76 Misc. Rep. 641, 137 N. Y. S. 243.

⁷¹Thompson's Ex. v. Thompson, (1920) 190 Ky. 3, 226 S. W. 350.

⁷²Frost v. Frost, (1909) 202 Mass. 100, 88 N. E. 446.

⁷³Lewis v. Brotherhood Acci. Co., (1907) 194 Mass. 1, 79 N. E. 802.

⁷⁴Makowiec v. Prudential Ins. Co., (1929) 83 N. H. 547, 145 Atl. 269; Cockrell v. Cockrell, (1902) 79 Miss. 569, 31 So. 203.

⁷⁵Vance, Insurance, 2nd ed., 551-552.

*Life Insurance Co.*⁷⁶ The court stated as the basis for upholding an insurance trust that the legal title during insured's lifetime was in the trustee because the trustee was donee-beneficiary, even though the insured reserved the usual rights. The New Jersey cases requiring the insured to deal in accordance with the terms of the policy in eliminating the beneficiary were cited with approval, although apparently there were some Illinois cases that could hardly be reconciled with this view. The court, though concluding the trustee was donee-beneficiary, also said the trustee was no mere beneficiary since it was named pursuant to a contract under seal and for a valuable consideration. The trustee was found to have rights as a bailee during the insured's lifetime so as to be qualified to maintain an action in trover, and to receive the proceeds. The court thus in a way recognized the dual character of a life insurance policy, though the insured apparently was not deemed by the court to have had any rights until he took certain precedent action.

Policies are quite often placed in trust by assignment. In such a case, a testamentary problem generally will not arise, but it may arise if the insured does not complete the assignment, or if the assignment contains a reservation of substantial rights in the insured. An assignment generally is recognized to be a transfer of property rights rather than an exercise of a power to appoint.⁷⁷ However, there is not a well defined rule on this subject. Sometimes an assignment is said to cut out the beneficiary. Sometimes it is said merely to grant a power to the assignee to change the beneficiary. Other cases hold it has no material effect on the beneficiary's rights.⁷⁸ If it is in effect a change of beneficiary, it is not entirely clear why the insured may not reserve rights as he does in a beneficiary case without the assignment as such being testamentary. But in general it may be expected that the courts will construe an assignment more strictly than they would a designation of a beneficiary since assignments do not have the exclusive insurance tradition back of them.

An assignment of a policy normally will be enforced if there has been delivery for a valuable consideration with the intent to

⁷⁶(1932), 268 Ill. App. 518, *supra* notes 44, 45, 60, 67.

⁷⁷*Mutual Benefit Life Ins. Co. v. Swett*, (C.C.A. 6th Cir. 1915) 222 Fed. 200.

⁷⁸*Henshaw, Rights of Beneficiaries as Affected by Assignments*, (1925) 3 *Ass'n of Life Insurance Counsel Proceedings* 45.

⁷⁹*Hewins v. Baker*, (1894) 161 Mass. 320, 37 N. E. 441.

vest title in the assignee.⁷⁹ This is so even though the interest involved is a contingent interest under a benefit certificate,⁸⁰ though there is some indication that it would be necessary to go into equity to enforce such an assignment.⁸¹ Assignments of policies are not testamentary even though payment is not to be made until the death of the insured.⁸² However, an assignment which reserved to the insured the right to make the choice of options contained in the policy, to receive the whole benefit without the consent of the assignee, and, in the event of the death of the assignee, to have the money payable to his estate, was held testamentary. The court said: "The deceased evidently desired to retain ownership to the last, and yet deprive his widow of her interest in his estate. This under our law he could not do."⁸³ It was also held that there had not been any such delivery of the instrument of assignment or of the policy as was necessary to constitute a transfer of any title legal or equitable. The purported assignee was declared to be a mere bailee since the papers placed in his possession were sealed and the contents thereof were not known to him. As to the trust involved, the court declared the same to be testamentary since it was not a present trust, divesting the insured of his ownership. A similar trust, based on assignments, was declared to be testamentary in a Massachusetts case⁸⁴ where the trustees according to the assignment paper were to be named in the will.⁸⁵ The court declared there was no delivery to the assignees and no intention that the assignor was holding for them.

An assignment to take effect in case the assignee survived the insured was held to be testamentary in the California case of *Mutual Benefit Life Ins. Co. v. Clark*.⁸⁶ In this case there was neither delivery of the policy nor of the assignment paper to the assignee, and the right was reserved to the assignor to revoke the

⁷⁹*Kimball v. Lester*, (1899) 43 App. Div. 27, 59 N. Y. S. 540, aff'd (1901) 167 N. Y. 570, 60 N. E. 1113; *Dexter v. Supreme Council*, (1904) 97 App. Div. 545, 90 N. Y. S. 292.

⁸¹*Jarvis v. Binkley*, (1903) 206 Ill. 541, 69 N. E. 582.

⁸²*Southern Mut. Life Ins. Ass'n v. Durdin*, (1908) 132 Ga. 495, 64 S. E. 264.

⁸³*Northwestern Mut. Life Ins. Co. v. Collamore*, (1905) 100 Me. 578, 62 Atl. 652.

⁸⁴*Frost v. Frost*, (1909) 202 Mass. 100, 88 N. E. 446.

⁸⁵One may declare a trust on the back of another's will as on any writing. *Fidelity Tit. & Trust Co. v. Graham*, (1918) 262 Pa. St. 273, 105 Atl. 295.

⁸⁶(1927) 81 Cal. App. 546, 254 Pac. 306.

assignment. There is authority contrary to the *Clark Case*.⁸⁷ It may be possible that where certain rights are reserved by the insured under an assignment such an assignment would be approved on the ground that the insured reserved to himself a life estate with the vested remainder in the policy contract in the assignee, subject to be divested by the assignee's prior death or the assignor's revocation. This concept is like that suggested regarding the dual character of the policy contract where the beneficiary's rights are involved.

In the *Gurnett Case*, previously mentioned,⁸⁸ the complainants conceded that if the policy had been placed in trust by an assignment it would have been proper. However, an assignment can raise the same difficult questions raised by the change of beneficiary method.

On the question whether delivery of the policies to the trustee has any bearing on the testamentary problem, it should be said that if the trustee is an assignee delivery should be made to complete the assignment and that the trust may be held to be testamentary if there is no delivery. But where the trustee is named as beneficiary, there appears no reason why delivery is necessary here any more than it is in any case when designating a beneficiary unless it is desired to raise an inference of an oral assignment. In the *Bose Case* the court said that whether the trustee had physical possession of the policies was wholly immaterial. The court in the *Gurnett Case*, however, when mentioning the rights of the trustee, noted that the trustee was a bailee and thus qualified to maintain an action of trover.⁸⁹ Possession of the policy would thus help to counteract to a certain extent the criticism that the trustee has no duties to perform during the lifetime of the insured. Withdrawing policies from the possession of the trustee in revoking the trust raises no particular problem, as the revocability of a trust does not per se make the trust testamentary.⁹⁰

⁸⁷*Burgess v. New York Life Ins. Co.*, (Tex. Civ. App. 1899) 53 S. W. 602.

⁸⁸(1932) 268 Ill. App. 518, supra note 76.

⁸⁹*Horton*, Life Insurance Trust Handbook 22.

⁹⁰*Jones v. Old Colony Trust Co.*, (1925) 251 Mass. 309, 146 N. E. 716; *Talbot v. Talbot*, (1911) 32 R. I. 72, 78 Atl. 535; *Robb v. Washington and Jefferson College*, (1906) 185 N. Y. 485, 78 N. E. 359. Cf. *Union Trust Company v. Hawkins*, (1929) 121 Ohio St. 159, 167 N. E. 389; *Warsco v. Oshkosh Savings and Trust Company*, (1924) 183 Wis. 156, 196 N. W. 829, holding revocable trusts to be testamentary where it was said the donors retained full control over the property.

No doubt there will be many more judicial declarations as to the problem of the testamentary character of life insurance contracts and trusts. It may be expected, however, that such declarations will follow along the lines of those made in the past,⁹¹ such as have been discussed here. Considering the trust origin of the rights of a beneficiary, and the later modifications in favor of the insured, a policy of insurance may be said to contain the elements of a mixed trust with rights in the beneficiary and as such will not be held to be testamentary.⁹² While the courts must be on their guard against a trust device in order to prevent evasion of the statute of wills so that creditors and heirs and the tax interest of the state may be protected, it should be noted that there is no special necessity for any such alertness in the insurance trust situation since the insured-settlor has been able to employ, and no doubt will continue to employ, the regular insurance arrangement without regard for creditor, heir or tax. The insurance trust is employed solely in the normal case for its administrative utility.

⁹¹See note (1933) 46 Harv. L. Rev. 818.

⁹²Professor Percy Bordwell of the College of Law, State University of Iowa, Iowa City, Iowa, wrote on April 19, 1933 to the author as follows: "... independently of authority, my reaction is that when a beneficiary is named there are the distinct elements of a trust in a life insurance policy, substantially, I mean, and not merely technically; and I think that it would be very advantageous to have that idea gotten over to insurers in general. It's a sort of mixed trust though, for where the insured has a right to make loans, and in these days I should say the word "puny" is inadequate to describe that right, he has a self-interest that would ordinarily be inconsistent with a trust. But I would say it is a new trust development and is just another example of the many forms the trust principle can take. If there are the elements of a trust, I don't believe there is much reason to question the validity of the transaction because of its mere testamentary character. There is nothing sacred about the requirements of the statute of frauds and wills, and my own reaction is that, if there is no obvious attempt to get away from the provisions of the statute of frauds and wills, one shouldn't worry too much about the testamentary character of the transaction. And if there are really trust elements involved, that is enough to my mind to answer the question of testamentary character . . . These are just off-hand reactions for what they are worth."